

Congress of the United States
Washington, DC 20515

April 26, 2023

The Honorable Jerome Powell, Chair
The Honorable Michael Barr, Vice Chair for Supervision
Board of Governors of the Federal Reserve System
20th Street & Constitution Avenue, NW
Washington, DC 20551

The Honorable Sandra Thompson
Director
Federal Housing Finance Agency
400 7th Street SW
Washington, DC 20219

The Honorable Martin Gruenberg, Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

The Honorable Gary Gensler, Chair
Securities & Exchange Commission
100 F Street, NE
Washington, DC 20549

The Honorable Michael Hsu
Acting Comptroller of the Currency
Office of the Comptroller of the Currency
Administration
400 7th St. SW
Washington, DC 20219

The Honorable Todd Harper
Chairman of the Board
National Credit Union
1775 Duke Street
Alexandria, VA 22314

Dear Chair Powell, Vice Chair Barr, Chairman Gruenberg, Acting Comptroller of the Currency Hsu, Chair Gensler, Director Thompson, and Chairman Harper:

The recent failures of Silicon Valley Bank (“SVB”) and Signature Bank have caused us to, once again, revisit the structures and riskiness of our nation’s banking sector. While the events of these two failures continue to unfold, what has already been made clear is Greg Becker, the disgraced Chief Executive Officer (CEO) of SVB, sold millions of dollars’ worth of stock options in the weeks leading up to the bank’s collapse, and employees of the failed institution took regularly scheduled bonuses and payouts almost immediately prior to the FDIC’s takeover.¹

Unfortunately, these circumstances cause us to, once again, raise the important questions of whether the incentive-based pay structures at SVB helped fuel the institution’s demise, and whether similar compensation structures—currently in place for executives at other financial institutions—can jeopardize the safety and security of America’s financial system going forward.

¹ Jacobs, Emily. “SVB collapse: CEO cashed out millions while employees got bonuses”. *Washington Examiner*. (March 11, 2023). <https://www.washingtonexaminer.com/policy/economy/svb-ceo-stock-sales-employee-bonuses> (Last Reviewed: March 26, 2023). Also See: Son, Hugh. “Silicon Valley Bank employees received bonuses hours before government takeover”. *CNBC*. (Published: March 11, 2023; Updated: March 12, 2023). <https://www.cnn.com/2023/03/11/silicon-valley-bank-employees-received-bonuses-hours-before-takeover.html>. (Last Reviewed: March 26, 2023).

President Biden has called for tightening the rules on claw backs and executive pay at failed financial institutions,² and Representative Maxine Waters, Ranking Member on the House Financial Services Committee, has stated a desire for your agencies to finalize the joint rulemaking under Section 956 of the Dodd-Frank Act by end of the year.³ Senator Sherrod Brown, Chairman of the Senate Banking Committee, has expressed similar concerns for the egregious risk-taking behaviors demonstrated in the wake of recent bank failures, and has called for stronger regulations on bankers' executive compensation. We share these concerns and urge you to finalize the Section 956 rulemaking by the end of the year.

Section 956 of the Dodd-Frank Act⁴ governs executive incentive-based compensation arrangements at covered financial institutions and specifically charges each of your agencies to "jointly prescribe regulations or guidelines that prohibit any types of incentive-based payment arrangement, or any feature of any such arrangement, that the regulators determine encourages inappropriate risks by covered financial institutions."⁵ According to the statute, your agencies were required to issue a finalized rulemaking no later than nine months after date of enactment.⁶ It has been more than twelve years since the passage of Dodd-Frank, and while two iterations of the rule have been proposed, a finalized rulemaking has yet to be issued.

According to publicly available information, executive compensation at SVB soared as the bank's profitability continued to skyrocket. From 2019 to the end of 2020, the bank's assets rose from \$70 billion to \$114 billion, and then again to about \$209 billion at the end of 2021.⁷ Over that same period, Mr. Becker's cash bonus rose to \$3 million in 2021 with a total yearly payout of \$10 million for 2021—a nearly sixty per cent increase over what Mr. Becker received just four years earlier.⁸ For 2022, Becker was awarded a \$1.5 million cash bonus and nearly \$10 million in overall pay.⁹

Mr. Becker was able to significantly increase his compensation award year-over-year due to the fact that his bonus awards were tied to the bank's return on equity, which rose dramatically between 2017 and 2021.¹⁰ Unfortunately, this compensation structure likely also encouraged

² Kinery, Emma. "Biden Calls on Congress to tighten laws to claw back executive pay, levy penalties in bank failures." *CNBC*. <https://www.cnn.com/2023/03/17/biden-calls-on-congress-to-tighten-rules-to-claw-back-executive-pay-levy-penalties-in-bank-failures.html>. (Published on: March 17, 2023, at 11:52 AM EDT; Updated: March 17, 2023 at 4:32 PM EDT) (Last Reviewed: March 26, 2023).

³ U.S. House Committee on Financial Services, Democrats. "Ranking Member Waters Announces Legislation in Progress to Strengthen Administration's Authorities on Clawbacks and Penalties, Urges Regulators to Finish Rules and Use Existing Authorities to Hold Executives Accountable Following Bank Failures." (March 17, 2023). <https://democrats-financialservices.house.gov/news/email/show.aspx?ID=VVT3WOUKD6YSZB23YSE36HA10M>.

⁴ Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, tit. IX, § 956, (codified at 12 U.S.C. 5641).

⁵ *Id.*

⁶ *Id.*

⁷ U.S. Committee on Financial Services, Ranking Member Waters. "Background on Recent Bank Failures." *U.S. Committee on Financial Services, Ranking Member Waters*. Pg. 2. (Updated and Distributed to Staff on March 22, 2023).

⁸ Gara, Antoine. <https://www.ft.com/content/02ff2860-2d5b-4e21-96af-cef596bff58e>.

⁹ *Id.*

¹⁰ Gara, Antoine. Temple-West, Patrick. and Tabby Kinder. "Executive pay at Silicon Valley Bank soared after big bet on riskier assets." *Financial Times*. (March 24, 2023). (Last Reviewed: March 24, 2023). <https://www.ft.com/content/02ff2860-2d5b-4e21-96af-cef596bff58e>.

recklessness. When in 2022 it appeared that SVB was headed for negative net income, SVB terminated hedges on interest rate risk. This boosted net income and executive pay based on return on equity. One observer noted: “Essentially, to juice its P&L [profit and loss] in the short term, SVB ambled into 2023 almost completely unhedged — in effect, a massive multibillion-dollar bet that interest rates were approaching their peak.”¹¹ Unfortunately, as we have all come to find out, this strategy backfired when interest rates rose and depressed the value of long-term Treasuries.

The connection between Mr. Becker’s massive compensation awards between 2017 and 2022 and the bank’s overall growth strategy over that same period leaves many of us to wonder: had the incentive-based compensation rules under Section 956 been finalized would the failure of SVB been avoided.

Therefore, we are writing to you today to encourage you to finalize the Section 956 rulemaking and include the following requirements, which will help align the compensation incentives of a financial institution’s executives with those of its customers, depositors, and the overall American public:

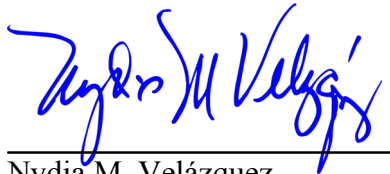
- Require deferral amounts of 100 percent of incentive-based compensation for both senior executives and significant risk-takers at all covered institutions. For a deferral period to have sufficient incentive effects, it must be longer than a financial institution’s typical credit cycle and make executives personally pay for the costs of their own recklessness.
- A ban on stock options in executive compensation packages. As has been demonstrated by the dramatic rise and fall of SVB, stock options provide executives like Mr. Becker with all the benefits of share price increases with none of the risks associated with share price decline. Research has indicated that because the payoffs from holding stock options are positively related to volatility of stock returns, options create incentives for executives to increase the volatility of share prices by engaging in riskier activities.
- A ban on hedging of bonus pay. Executives like Mr. Becker can purchase insurance or other hedging instruments to cover their downside risk from company performance. For incentives of a long-term deferral period to be effective, individual employees must be prohibited from hedging their own compensation.

¹¹ Robin Wigglesworth, How Crazy Was Silicon Valley Bank’s Zero-Hedge Strategy? FINANCIAL TIMES, (March 17, 2023).

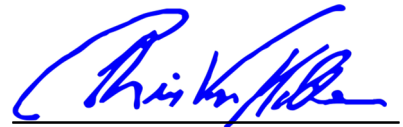
As we sift through the failures of another American bank and another apparent example of the bank's CEO and senior executives pursuing a strategy for their own enrichment at the apparent expense of the bank's overall health, it is clear that it is well past time to change the culture and incentives for the industry's top executives. We must change these motivations to avert a similar disaster in the future. It is time for your agencies to finalize the Section 956 rulemaking.

We appreciate your attention to this matter.

Sincerely,

A handwritten signature in blue ink, appearing to read "Nydia M. Velázquez", written over a horizontal line.

Nydia M. Velázquez
Member of Congress

A handwritten signature in blue ink, appearing to read "Chris Van Hollen", written over a horizontal line.

Chris Van Hollen
United States Senator